MULTIMEDIA UNIVERSITY

STUDENT ID NO

MULTIMEDIA UNIVERSITY

FINAL EXAMINATION

TRIMESTER 1, 2022/2023 (TERM ID 2210 & TERM ID 2215)

BBF2124 – FINANCIAL MANAGEMENT II

(All sections / Groups)

16 FEBRUARY 2023
9.00 a.m -11.00 a.m
(2 Hours)

INSTRUCTIONS TO STUDENT

1. This question paper consists of 3 pages with 4 Questions only.
2. Answer **ALL** questions.
3. The distribution of the marks for each question is given at the end of each question.
4. Please write all your answers in the Answer Booklet provided. Start each answer on a new page.

QUESTION 1

Kavana Corporation is attempting to determine whether to purchase or lease a new machine. The firm is in the 40% tax bracket, and its after-tax cost of debt is currently 8%. The terms of the lease and purchase are as follows:

Lease Annual end-of-year lease payments of RM25,200 is required over the 3-year life of the lease. All maintenance costs will be paid by the lessor; insurance and other costs will be borne by the lessee. The lessee will exercise its option to purchase the asset for RM5,000 at termination of the lease.

Purchase The machine, costing RM60,000, can be financed entirely with a 14% loan requiring annual end-of-year payments of RM25,844 for 3 years. The firm in this case will depreciate the machine under MACRS using a 3-year recovery period. (Please refer to Table 1 in the Appendix for the applicable depreciation percentages.) The firm will pay RM1,800 per year for a service contract that covers all maintenance costs; insurance and other costs will be borne by the firm. The firm plans to keep the machine and use it beyond its 3-year recovery period.

(a) Calculate the *after-tax cash outflows* of Kavana Corporation under each alternative. (10 marks)

(b) Calculate the present value of each cash outflow stream, using the after-tax cost of debt. (10 marks)

(c) Which alternative, either lease or purchase would you recommend to Kavana Corporation? Please explain why. (5 marks)

(Total: 25 marks)

QUESTION 2

(a) A share repurchase is a transaction whereby a company buys back the shares from the marketplace.

(i) Identify and briefly explain on **THREE (3)** most common methods of executing a share repurchase program. (9 Marks)

(ii) Who are holders of record? When does a stock sell ex dividend? (6 Marks)

(b) Trademark Companies has 25,000 shares of common stock outstanding, retained earnings of RM40,000 which include the current year's earnings and RM 800,000 in paid up capital. In the current year, the firm has RM 29,000 of earnings available for the common stockholders.

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(i) Calculate the maximum cash dividend per share that the firm can pay to each common stockholder: (Assume that legal capital includes all paid-in capital). (5 Marks)

(ii) What would be the effect on the firm's balance sheet entries and retained earning if cash dividend decreases to $0.80 per share? (5 Marks)

(Total: 25 marks)

QUESTION 3

(a) Moffats Corporation has an outstanding issue of 15-year convertible bonds with a RM1,000 par value. These bonds are convertible into 80 shares of common stock. They have a 13% annual coupon interest rate, whereas the interest rate on straight bonds of similar risk is 16%.

(i) Calculate the straight bond value for Moffats Corporation. (6 Marks)

(ii) Calculate the conversion (or stock) value of the bond when the market price is RM9, RM12, RM13, RM15, and RM20 per share of common stock. (5 Marks)

(iii) For each of the common stock prices given in part (ii), at what price would you expect the bond to sell? Why? (5 Marks)

(iv) Draw a graph of the straight value and conversion value of the bond for each common stock price given. Use this graph to indicate the minimum market value and market premium of the bond associated with each common stock price. (5 Marks)

(b) Briefly explain on **TWO (2)** differences between Stock Warrants and Stock Options. (4 Marks)

(Total: 25 marks)

QUESTION 4

(a) Arfan Inc. is a holding company that has voting control over both Mini Stores and Shooting Stores. Arfan owns Mini Stores and Shooting Stores common stock valued at RM15,000 and RM12,000, respectively. Mini's balance sheet lists RM130,000 of total assets, and Shooting has total assets of RM110,000. Arfan has total common stock equity of RM20,000.

(i) What is the percentage of the total assets controlled by Arfan Inc.? (7 Marks)

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(ii) If a stockholder holds RM5,000 worth of Arfan Inc common stock equity and this amount gives this stockholder voting control, what percentage of the total assets controlled does this stockholder's equity investment represent? (6 Marks)

(b) Briefly explain on the terms below:
(i) Trading Blocs (3 Marks)
(ii) Euromarket (3 Marks)
(iii) Spot exchange rate (3 Marks)
(iv) Eurobond (3 Marks)

(Total : 25 Marks)

Appendix

Table 1 MACRS Depreciation Table

	Percentage by recovery year*			
Recovery year	3 years	5 years	7 years	10 years
1	33%	20%	14%	10%
2	45	32	25	18
3	15	19	18	14
4	7	12	12	12
5		12	9	9
6		5	9	8
7			9	7
8			4	6
9				6
10				6
11				4
Totals	100%	100%	100%	100%

*These percentages have been rounded to the nearest whole percent to simplify calculations while retaining realism. To calculate the *actual* depreciation for tax purposes, be sure to apply the actual unrounded percentages or directly apply double-declining balance depreciation using the half-year convention.

(Source: Gitman, Lawrence J. and Zutter, Chad J. Principles of Managerial Finance, 14th Edition, Global Edition (2015), Pearson, Boston)

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